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SUBJECT: South China Economic Analysts Predict Continued Reliance on Exports, Exchange Rate Stability

REF: A) 09 Guangzhou 237; B) 08 Guangzhou 406

GUANGZHOU 00000077 001.2 OF 002

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11. (SBU) Summary and comment: Although China is making gradual progress towards greater economic diversification, cheap exports will continue to drive growth in the near term, according to comments made by local economic analysts during a conversation with the Consul General, visiting Deputy Director of the China Desk and Beijing Poloff on January 26. The recovery of overseas orders and the return to profitability for regional industries have not translated into higher wages for most workers, meaning that real estate and automobile prices are unaffordable for most local consumers. As new technology and higher value-added industries emerge, the recent multi-year import surge may lose some steam as firms develop local alternatives and cease importing higher-priced foreign goods. End summary and comment.

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EXPORTS STILL TOP BREADWINNER  
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12. (SBU) Guangdong Citibank Branch President Peter Qiu told us that despite thin margins and regulatory pressures to relocate out of their traditional Pearl River Delta base (refs A and B), low value-added manufacturing industries recovered enough in 2009 to continue operations. Neither domestic demand for surplus goods originally produced for export nor high-tech manufacturing output have been robust enough to reverse south China's reliance on export-oriented growth in the near term. Qiu commented that the government could be expected to take a more cautious approach to infrastructure stimulus, but it would likely continue with efforts to stimulate domestic consumption.

13. (SBU) While exports continue to be the major source of growth in China, there are also signs that a recent multi-year import surge may taper off as local production increasingly displaces imports. Price Waterhouse Coopers Partner Alfred Leung highlighted heavy machinery as an example of a good that was until recently imported

but is now increasingly produced locally. Qiu affirmed this analysis, noting that the displacement of exports to China from Southeast Asian countries had become a source of friction.

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EXCHANGE RATE DEFENSE KEY TO STABILITY  
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¶4. (SBU) Leung also commented that the defense of the current renminbi exchange rate should be seen as an effort to maintain economic stability rather than as a barrier to imports. Local oil and gas prices have been allowed to almost double in the last four years, even as domestic automobile sales surged in 2009 and wages failed to increase at the same rate as real estate prices, according to Leung. The resulting economic situation looked "almost like the economy is overheating," he said.

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SHIFTING MIGRATION, ENERGY USE PATTERNS  
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¶5. (SBU) Both Qiu and Leung said labor shortages had begun to develop in Guangdong-based manufacturing industries such as textiles and shoes towards the end of 2009. Flat wages, increased living costs and improved transportation infrastructure connecting manufacturing centers with newly developing inland areas have all caused a shift in migrant labor patterns such that laborers are now more likely to consider staying close to their rural hometowns than relocate to the Pearl River Delta. Guangdong Oil and Gas Association Secretary General Helen Liang added that energy consumption patterns also indicated a gradual migration of industrial output from traditional coastal centers to more inland areas. Liang said energy consumption had not recovered to pre-recession levels in the Pearl River Delta, but that inland areas

GUANGZHOU 00000077 002.2 OF 002

were showing signs of sustained growth.

¶6. (U) This cable was coordinated in draft with EAP/CM and Embassy Beijing.

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